No. 84-1274

IN THE

Supreme Court of the United States

OCTOBER TERM, 1985

BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM,
Petitioner,

v.

DIMENSION FINANCIAL CORPORATION, *et al.*,
Respondents.

On Writ of Certiorari to the United States Court of Appeals For the Tenth Circuit

BRIEF OF SEARS, ROEBUCK AND CO., ALLSTATE ENTERPRISES, INC., AND GREENWOOD TRUST COMPANY AS AMICI CURIAE IN SUPPORT OF RESPONDENTS

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QUESTION PRESENTED

Sears, Roebuck and Co. and its affiliates, Allstate Enterprises, Inc. and Greenwood Trust Company, will address the following question: Whether the Congress of the United States, in enacting and amending the Bank Holding Company Act, 12 U.S.C. §§ 1841 *et seq.*, intended to establish and implement a national policy of separating banking and commerce.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Table of Authorities Continued

Table of Authorities Continued

Table of Authorities Continued

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INTEREST OF THE AMICI CURIAE

This case concerns the power of the Board of Governors of the Federal Reserve System (the "Board"), acting under authority purportedly conferred by the Bank Holding Company Act as amended, 12 U.S.C. §§ 1841 *et seq.* (the "BHCA" or the "Act"), to redefine (through the Board's Regulation Y, 12 C.F.R. § 225) specific terms in § 2(c) of the BHCA, 12 U.S.C. § 1841(c).[1] Such redefinition, if allowed to stand, will bring within the Board's regulatory authority the corporate owners of depository institutions that had not previously been defined as "banks"

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[1] *See infra* note 16.

within the meaning of the Act. These institutions are characterized by the Board as "nonbank banks," but are referred to herein as "non-BHCA banks."[2]

Sears, Roebuck and Co., through its subsidiary Allstate Enterprises, Inc., controls the Greenwood Trust Company (together, "Sears"), an insured non-BHCA bank chartered in the State of Delaware that makes no commercial loans. The Board's brief makes clear that its intention in amending Regulation Y is to hinder the development of such non-BHCA banks. If successful, the Board's action will have a substantially adverse impact on Sears, on its financial services business, and on the financial services alternatives made available to the American consumer by Sears and other diversified financial services firms.

Sears is particularly concerned that the Board, having repeatedly failed to obtain approval of Congress for the expansion of its authority with respect to non-BHCA banks, is seeking to achieve such an expansion through unilateral administrative fiat, advancing in support of its action the myth that the BHCA implements a national policy of separating banking and commerce. Because the adoption by this Court of the Board's view of the BHCA would harm Sears, as well as the interests of consumers, Sears believes it can offer this Court a useful perspective on whether Congress intended in the BHCA to separate banking and commerce or intended in general to apply the Act to institutions other than commercial banks as Congress carefully and narrowly defined that term in 1970.

This brief is filed pursuant to Rule 36.2 of the Rules of this Court. The parties have consented to the filing of this brief. Their letters of consent have been filed with the Clerk of the Court.

INTRODUCTION

Central to the Board's argument in this case is its assertion that the BHCA is "a comprehensive federal framework" to

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[2]*See infra* note 17.

implement a "national polic[y] requiring a separation of banking and commerce in this country...." *See* Pet. Br. at 2-3, 10, 12, 13, 16, 18, 20. This contention allows the Board to link its actions to an alleged congressional policy and thereby to claim for itself a range of authority that it has been repeatedly denied by Congress. In fact, however, Congress never intended to establish, and has not established, a national policy of separating banking and commerce.

Since at least 1943, the Board has regularly urged Congress to "separate banking and commerce" by restricting, and authorizing the Board to regulate, the activities of organizations that own or control all depository institutions.[3] Despite the Board's repeated requests, Congress has consistently refused to draw a line between banking and commerce; instead, the actions of Congress have been far more limited, reflecting almost entirely a desire to constrain the economic power of commercial banks.

When Congress has acted, it has addressed specific manifestations of this power as they arose, going no further than necessary to achieve its limited objectives. Its actions have reflected a careful balancing of the Board's requests for sweeping authority to separate banking and commerce with a sensitive concern for maintaining competition and flexibility in the economy.

Integral to achievement of these congressional goals is the definition of "bank" in the BHCA. In defining that term, Congress evinced a keen awareness of the term's significance as the fulcrum of the Board's jurisdiction. When enacted in 1956, the Act was intended to include only commercial banks,[4] but failed to implement this intent clearly.[5] Consequently, Congress amended the definition in 1966 and again in 1970, each time

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[3]*See infra* pp. 9-10.

[4]102 *Cong. Rec.* 6,857 (1956) (statement of Sen. Robertson).

[5]"Bank" was defined by the 1956 Act as "any national banking association or any State bank, savings bank, or trust company. . . ." Bank Holding Company Act of 1956, Ch. 240, § 2(c), 70 Stat. 133, 12 U.S.C. § 1841(c)(1)(1956).

narrowing the statutory language so that the BHCA could be applied by the Board only to the holding companies of what Congress repeatedly referred to as "commercial banks."[6]

The Board simply asserts in its brief that the depository institutions which it brought within the BHCA by revising Regulation Y are commercial banks. *See* Pet. Br. at 21. But this assumes the issue the Board is required to prove. As this brief will show, by adopting a specific and literal test for defining commercial banks in 1966 and 1970, Congress clearly reserved to itself the authority to expand the reach of the BHCA to other depository institutions. This Court should reject the Board's attempt to overreach its limited mandate and usurp the exclusive power of Congress to determine national banking policy through plenary legislation.

SUMMARY OF ARGUMENT

As originally enacted in 1956, the BHCA applied *only* to companies that owned two or more institutions chartered as banks under state or federal law.[7] This permitted the continued ownership of banks by commercial firms and the continued acquisition by one-bank holding companies of nonbanking businesses. Many such relationships were then in existence.[8] The Board urged Congress in 1955 to include holding companies of a single bank in the proposed legislation, asserting that only in this way could banking and commerce be separated.[9] Congress refused to do so. The legislative history of the 1956 Act shows clearly that Congress was concerned principally with limiting

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[6]*See, e.g.*, S. Rep. No. 1084, 91st Cong., 2d Sess. 24 (1970) (definition changed because the 1966 definition included "institutions which are not in fact engaged in commercial banking"); S. Rep. No. 1179, 89th Cong., 2d Sess. 7 (1966) (redefinition needed to avoid covering companies not commercial banks).

[7]Ch. 240, § 2(a), 70 Stat. 133, 12 U.S.C. § 1841(a)(1)(1956).

[8]*See infra* note 25.

[9]Statement of William McChesney Martin, Jr., Chairman, Board of Governors, Federal Reserve System, *Control and Regulation of Bank Holding Companies: Hearings on H.R. 2674 before the House Committee on Banking and Currency*, 84th Cong., 1st Sess. 15 (1955).

the economic power of a few large multi-bank holding companies of commercial banks and not otherwise disturbing existing relationships involving only a single bank.[10]

Congress addressed the BHCA again in 1966, deleting some of the exemptions for multi-bank holding companies it had adopted in 1956. Once again, the Board urged Congress to separate banking and commerce by applying the Act to the holding companies of a single bank.[11] Congress again refused. S. Rep. No. 1179, *supra* note 6, at 5.

For purposes of the issue now before this Court, the most significant element of the 1966 amendments was a change in the definition of bank. Congress: (i) overruled a 1963 Board interpretation that used a functional ("actual practice") test to bring the corporate owners of industrial banks within the coverage of the Act, 49 Fed. Res. Bull. 166 (1963); (ii) rejected compromise language advanced by the Board;[12] and (iii) substituted a specific definition of bank that reduced the Board's interpretive latitude by focusing on the legal rights of the depositor. Congress stated clearly that its purpose in redefining the term bank in 1966 was to make wholly clear that the BHCA was intended to apply only to the holding companies of commercial banks. S. Rep. No. 1179, *supra* note 6, at 7.

Between 1966 and 1970, the issue for Congress changed considerably. Using the one-bank holding company format, large commercial banks began to expand into nonbanking activities. Concern developed in Congress that the substantial economic power of large commercial banks would be enhanced in a new way: by providing preferential financing to commercial enterprises affiliated with these banks through holding companies. S. Rep. No. 1084, *supra* note 6, at 2-4. This impelled

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[10]*See* S. Rep. No. 1095, 84th Cong., 1st Sess. 7-8, 12 (1955); *see also* 102 *Cong. Rec.* 6,936 (1956) (statement of Sen. Fulbright).

[11]Statement of William McChesney Martin, Jr., Chairman, Board of Governors, Federal Reserve System, *Amend the Bank Holding Company Act of 1956: Hearings on S.2353, S.2418 and H.R. 7371 Before Subcomm. of the Senate Committee on Banking and Currency*, 89th Cong., 2d Sess. 58 (1966).

[12]*See infra* note 29.

Congress in 1970 to extend the BHCA to the holding companies of a single commercial bank. In doing so, however, Congress provided more latitude for bank holding companies to expand and compete in areas of commerce "closely related to banking" in which banks themselves traditionally could not engage.[13] Once again, the consistent theme of congressional action was not the separation of banking and commerce but the imposition of statutory constraints on the economic power of commercial banks.

That Congress has never intended to establish a policy of separating banking and commerce is further demonstrated by its actions since 1970. For example, in the Garn-St Germain Act of 1982 ("Garn-St Germain"),[14] Congress authorized federal savings and loan associations and savings banks to exercise the traditional powers of commercial banks by making commercial loans and establishing demand deposits for their commercial loan customers.[15] If Congress were truly concerned about "separating banking and commerce," as the Board asserts, surely it would have applied that policy to a class of institutions that it had authorized to exercise all the powers of commercial banks. However, Congress did not take this step. Instead, Garn-St Germain specifically exempted these institutions from the "comprehensive framework" of the BHCA, permitting their affiliates to be regulated only by the Savings and Loan Holding Company Act, 12 U.S.C. §§ 1730a *et seq.*, which imposes no restrictions on the activities of a company that owns or controls a single savings and loan association or federal savings bank. *See infra* note 43.

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[13]*See, e.g.*, 116 *Cong. Rec.* 42,422 (1970) (statement of Sen. Sparkman) (Amendments provide greater regulatory flexibility).

[14]Garn-St Germain Depository Institutions Act of 1982, Pub. L. No. 97-320, 96 Stat. 1469 (1982).

[15]*Id.* at § 312, 96 Stat. 1469, 1496, 12 U.S.C. § 1464(b) (1985) (authority to establish demand deposits for commercial loan customers); *id.* at § 325, 96 Stat. 1469, 1500, 12 U.S.C. § 1464(c)(1) (authority to make commercial loans).

The actions of Congress thus squarely refute the Board's assertion that Congress has established, in the BHCA or otherwise, a "comprehensive federal framework" to implement a "national polic[y] requiring a separation of banking and commerce in this country."

ARGUMENT

The Bank Holding Company Act Was Not Intended To Separate, and Has Not Separated, Banking and Commerce

In attempting to justify a reversal of its longstanding interpretation of Section 2(c) of the BHCA, 12 U.S.C. § 1841(c) (1985)[16], the Board rationalizes and defends its actions by arguing that Congress intended through the BHCA to effect the "separation of banking and commerce." This convenient and imprecise phrase is offered to portray non-BHCA banks[17] as

[16]In a series of decisions culminating in the promulgation in January 1984 of a revised Regulation Y under the BHCA, the Board reversed positions it had taken over many years concerning the meaning of the term "bank," defined under section 2(c) of the BHCA as any institution that "(1) accepts deposits that the depositor has a legal right to withdraw on demand, and (2) engages in the business of making commercial loans." *Compare* the Board's new position under Regulation Y *with, e.g.*, its approval of the acquisition and operation by a subsidiary of the large commercial firm, Gulf & Western Industries, Inc., of the Fidelity National Bank (later renamed Associates National Bank). *See* Bank Admin. Institute Innerline, Index of Bank Performance (1982) (J.A. 108A).

[17]Non-BHCA banks are characterized, in the Board's brief and elsewhere, as "nonbank banks." This terminology may convey the misleading impression that these institutions are somehow extralegal and not otherwise subject to federal or state laws governing the activities of depository institutions. However, depository institutions that do not meet the definition of bank in Section 2(c) of the BHCA are in all other respects banks within the meaning ordinarily ascribed to that term. Thus, these institutions are chartered under state or federal law, regulated by state and federal bank regulatory authorities, fully subject to all applicable federal and state laws governing depository institutions, eligible for federal deposit insurance, and for the most part offer deposits insured by the Federal Deposit Insurance Corporation. *See, e.g.*, 12 U.S.C. § 1818 (regulatory powers of the FDIC for all "insured banks," including cease-and-desist orders); Cal. Fin. Code §§ 1900-1914 (Deering 1985) (banks); Cal. Fin. Code §§ 18390-18393 (Deering 1985) (industrial loan companies); N.Y. Banking Law § 14 (McKinney 1985); Va. Code §§ 6.1-3 to 6.1-125 (1985) (banks); and Va. Code §§ 6.1-227 to 6.1-242 (1985) (industrial loan associations).

"evasions" of the Act, *see, e.g.*, Pet. Br. at 11, and to provide otherwise nonexistent legislative authorization for the Board's functional construction of language carefully chosen by Congress to confine the Board's jurisdiction.

As the following discussion will show, the Board's premise is a fiction. The BHCA, at its inception and in each of its amendments, reflects a series of attempts by Congress to limit the economic power of the nation's commercial banks; it was not at its enactment and is not today a statute that "separates banking and commerce." Congress has never adopted the Board's expansive slogan as an expression of national policy.[18] Congressional actions, on the contrary, especially when viewed in the context in which they were taken, were specific and narrowly tailored, intended to restrict the perceived economic power of commercial banks, while leaving other sectors of the financial economy free to compete.

The Board's arguments concerning the alleged dangers of non-BHCA banks are neither unique to this case nor confined to the judicial branch. The Board has made substantially the same arguments to Congress over the past four years, all as part of an unsuccessful effort to obtain legislation that would close what the Board chooses to characterize as the "nonbank bank loophole."[19] In advancing these arguments before this Court, the Board is simply seeking to obtain from the judiciary

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[18]In reviewing the legislative history of the BHCA, care should be taken not to confuse rhetoric incorporating the catch-phrase "separation of banking and commerce" with a national policy actually adopted by Congress. The phrase was frequently employed in the legislative history of the BHCA. *See, e.g.* Individual Views of Rep. Patman, H.R. Rep. No. 387, 91st Cong., 1st Sess. 27 (1969); 115 *Cong. Rec.* 33,132 (1969) (statement of Rep. Boland); S. Rep. No. 1179, *supra* note 6, at 2-3; 102 *Cong. Rec.* 6,853 and 6,919 (1956) (statements of Sens. Robertson, Barkley and Capehart); 102 *Cong. Rec.* 6,936 (1956) (statement of Sen. Fulbright). It is, however, the substance of statutes enacted by Congress, not catch-phrases or slogans, that establishes and implements a national policy.

[19]*See, e.g.*, P. Volcker, Statement before the Subcommittee on Financial Institutions, Supervision and Regulation of the House Committee on Banking, Finance and Urban Affairs 1 (April 17, 1985).

an objective—control over all companies that own depository institutions—that it has repeatedly been denied by Congress.

A. The Board's Early Attempts to Obtain Legislation

Prior to 1933, there was no federal restriction on the common ownership of banks and commercial firms. The first such restriction appeared in the Banking Act of 1933 (the Glass-Steagall Act), which restricted the ability of a company to own both a Federal Reserve member bank and an investment banking firm.[20] In 1938, 1941, 1945, 1947, 1949, 1950, 1953 and 1954 the Board unsuccessfully urged more comprehensive legislation. *See* S. Rep. No. 1095, *supra* note 10, at 3-4. In 1943, for example, the Board articulated its case for more authority in the following terms:

> There is now no effective control over the expansion of bank holding companies either in banking or in any other field in which they may choose to expand. Moreover, the device lends itself readily to the amassing of vast resources obtained largely from the public which can be controlled and used by a few people and which give to them, when they choose so to use them, an unfair and overwhelming advantage in acquiring additional properties and in carrying out an unlimited program of expansion. . . . The Board believes, therefore, that it is necessary in the public interest and in keeping with sound banking principles that the activities of bank holding companies be restricted solely to the banking business and that their activities be regulated, as are the activities of the banks themselves. . . . [T]he Board recommends that immediate legislation be enacted preventing further expansion of existing bank holding companies or the creation of new bank holding companies.

30 *Annual Report of the Board of Governors* 37 (1943).

Congress was not moved by this or similar appeals. Only in 1956, after the courts rejected the Board's effort to apply the

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[20]Banking Act of 1933, Ch. 89, §§ 16 and 19, 48 Stat. 162, 184-85 and 188.

Clayton Act to Transamerica Corporation — then the nation's largest multi-bank holding company — did Congress provide the Board with additional authority over bank holding companies by enacting the BHCA. *Transamerica Corp. v. Board of Governors of Federal Reserve System*, 206 F.2d 163 (3d Cir. 1953).

B. The BHCA of 1956

The Board had sought unsuccessfully to control the expansion of the Transamerica Corporation since the early 1940s. *See* Cagill, *Branch, Chain and Group Banking* in *Banking Studies* 131-38 (1941). *See generally Peoples Bank v. Eccles*, 161 F.2d 636 (D.C. Cir. 1947), *rev'd on other grounds*, 333 U.S. 426 (1948). Finally, in 1952, the Board instituted Clayton Act proceedings against Transamerica in an effort to break up that corporation's control of banks in five Western states.

The Third Circuit set aside the Board's divestiture order. Although Transamerica controlled 645 commercial banking offices in a five-state area — representing 41% of all such offices and 39% of all commercial bank deposits — the Board's determination in another context that the "business of commercial banks is largely local" was found by the court to be inconsistent with the Clayton Act's "substantially lessen competition" test. 206 F.2d, at 167-70.

Debate in Congress on the BHCA focused heavily on the dangers Congress saw in the growth of Transamerica.[21] Congress viewed Transamerica's nonbanking activities, and those of other multi-bank holding companies, as a means by which the commercial banking power of these holding companies

[21]*See, e.g.*, 102 *Cong. Rec.* 6,943 (1956) (statement of Sen. Morse) (bill "primarily aimed" at Transamerica); H. R. Rep. No. 609, 84th Cong., 1st Sess. 9, 17 (1955) (Transamerica a "concrete illustration" of the potential abuses arising out of bank holding companies with large banking assets).

might be enhanced, to the detriment of independent banks.[22] The Act was described in congressional reports not as an effort to separate banking and commerce but as a bill to promote fair competition and prevent the abuse of commercial credit power.[23]

As enacted, the BHCA covered only companies that owned two or more "banks," a term which was defined broadly to include any institution chartered as a bank under federal or state law. The scope of the BHCA was sharply limited by the multi-bank requirement, and by a number of significant exemptions that removed several large multi-bank holding companies from its coverage. Thus, of the 163 companies that owned at least one bank in 1956, only 44 were multi-bank holding companies subject to the Act. Of these 44 multi-bank holding companies, many were exempted entirely from the Act, and it appears that only six, including most notably Transamerica, were required to divest those nonbanking businesses that did not conform to statutory requirements.[24]

[22]For example, in opposing an amendment that would have allowed multi-bank holding companies to continue to hold all of their nonbanking assets, Senator Robertson stated:

> The very object of the independent bankers would be defeated, which is to break up the combination between banking assets, on the one hand, and a vast industrial expansion on the other, where the overlord, the holding company, can pump assets into one branch or bank to stifle competition, against the interest of the local people.

102 *Cong. Rec.* 6,920 (1956).

See also 102 *Cong. Rec.* 6,861-62 (1956) (statement of Sen. Payne) (vast capital resources behind a subsidiary bank an "undeniable competitive advantage" against independent banks).

[23]*See, e.g.*, H.R. Rep. No. 609, *supra* note 22, at 2-6 (describing the "four fundamental reasons" for enacting the legislation: (i) preventing concentration of banking resources, (ii) stopping circumvention of state laws against interstate banking, (iii) preventing potential abuses of credit powers, and (iv) fostering competitive banking).

[24]*See* Note, *The Bank Holding Company Act of 1956*, 9 Stan. L. Rev. 333, 347-48 (1957).

Because it applied only to multi-bank holding companies, the BHCA as initially adopted did not separate banking and commerce. Of the 119 one-bank holding companies that were not covered by the Act, many were diversified commercial firms that owned a single bank.[25] The Board protested this exclusion, arguing for a true separation of banking and commerce, but the Senate Banking Committee could find no reason to take this step. *See* S. Rep. No. 1095, *supra* note 10, at 7. On the contrary, Congress was concerned that including one-bank holding companies would probably result in the forced sale of large numbers of small banks and therefore in the diminution of competition.[26]

The real focus of congressional concern was the concentration of commercial credit power in multi-bank holding companies and not the abstract concept of separating banking and commerce. The Senate Committee Report made this clear:

> Your committee did not deem it necessary to include within the scope of this bill any company which manages or controls no more than a single bank. It is possible to conjure up visions of monopolistic control of banking in a given area through ownership of a single bank with many and widespread branches. However, in the opinion of your committee, no present danger of such control through the bank holding company device threatens to a degree sufficient to warrant inclusion of such a company within the scope of this bill.

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[25]One hundred and sixty-three bank holding companies existed as of 1956, many with large nonbanking businesses. Among those which continued to be exempt from federal regulation after the Act were W. R. Grace & Co., Deere & Co., Corn Products Refining Co., Gimbel Bros., Inc., and Equity Corp. (which owned Bell Aircraft Corp., four other industrial corporations, a real-estate company, and an oil company). *See* 102 *Cong. Rec.* 6,942 (1956) (statement of Sen. Morse). *See generally Control of Bank Holding Companies: Hearings Before a Subcommittee of the Senate Committee on Banking and Currency on S. 850, S. 2350, and H.R. 6276*, 84th Cong., 1st Sess. 51-60 (1955) (listing all bank holding companies as of that time).

[26]*See* Chase, *The Emerging Financial Conglomerate: Liberization of the Bank Holding Company Act*, 60 Geo L.J. 1225, 1232-33 (1972).

S. Rep. No. 1095, *supra* note 10, at 7.

C. 1966 Amendments

The passage of the BHCA did not diminish the Board's enthusiasm for expanding its regulatory authority to *all* holding companies of depository institutions, and it continued its campaign under the banner of separating banking and commerce.[27]

Congress ignored the Board's requests for more authority until 1966. In hearings on bills to amend the 1956 Act, the Board's then Chairman, William McChesney Martin, Jr., advocated that the BHCA be extended to one-bank holding companies in order to effect the separation of banks from nonbanking businesses:

> The first [objective of the BHCA] is to prevent undue concentration of control over banks in the hands of any holding company, and the second is to prevent any holding company from controlling both banks and nonbanking businesses . . . . While there would obviously be no need for the act to cover one bank holding companies if its only purpose were to prevent any holding company from acquiring too many banks it seems just as clear that coverage of one bank holding companies is necessary to accomplish the act's second objective.

Amend the Bank Holding Company Act of 1956: Hearings, *supra* note 11, at 58.

Congress, however, had much more limited objectives in mind. The 1966 amendments merely refined the BHCA as

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[27]On May 7, 1958, for example, it filed a special report with Congress which recommended, among other things, both the extension of the 1956 Act to one-bank holding companies and the repeal of some of the exemptions adopted in 1956. *See Report of the Board of Governors of the Federal Reserve System Pursuant to the Bank Holding Company Act of 1956* 8-15 (1958). *See generally* Savage, *A History of the Bank Holding Company Movement, 1900-78*, in Staff of the Board of Governors of the Federal Reserve System, *The Bank Holding Company Movement to 1978: A Compendium* 21, 51-52.

passed a decade earlier.[28] Congress again refused to adopt the Board's request that the Act be extended to one-bank holding companies. The Senate Banking Committee noted that the Board's approach might diminish rather than increase competition:

> [T]here was no substantial evidence of abuses occurring in one-bank holding companies. Furthermore, the committee received much testimony to the effect that repeal of the exemption would make it more difficult for individuals to continue to hold or to form small independent banks. The repeal of the exemptions would, therefore, be likely to result in causing the forced sale of large numbers of banks and in a diminution of competition rather than in an increase of competition. Consequently, the committee decided not to adopt this proposal.

S. Rep. No. 1179, *supra* note 6, at 5.

Significantly, and wholly consistent with the Act's purpose, Congress also used the occasion of the 1966 amendments to narrow the definition of "bank" so that the BHCA unambiguously applied only to *commercial* banks. The context of this action demonstrates clearly that Congress intended to reserve to itself the authority to extend the BHCA to other classes of depository institutions.

As initially adopted, the Act covered the holding companies of two or more "banks," defined as "any national banking organization or any State bank, savings bank, or trust company." Ch. 240 at § 2(c), 70 Stat. 133 (1956). In 1963, the Board attempted to place a functional ("actual practice") construction on this language. Although the Board admitted that the BHCA was intended to cover only commercial banks, 49 Fed. Res. Bull.

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[28]Among the major changes were the elimination of the 1956 Act's exemption for charitable trusts—thus permitting coverage of the Alfred I. duPont Trust, which owned or controlled 30 banks in Florida, *see* S.Rep. No. 1179, *supra* note 6, at 3-4—and the elimination of provisions in the 1956 Act which had restricted loans by a holding company bank to its affiliates. *See id.* at 10.

166 (1963), it sought to include industrial banks under the Act if:

> in a particular case, regardless of the title of the institution or the form of the transaction, it *accepts deposits subject to check or otherwise accepts funds from the public that are, in actual practice, repaid on demand,* as are demand or savings deposits held by commercial banks.

Id. (emphasis added).

Responding in 1966 to the ensuing protests of the industrial bank industry, Congress not only corrected this erroneous interpolation of its 1956 language but also rejected compromise language advanced by the Board that would have defined "bank" for purposes of the BHCA as any institution that accepts deposits "payable on demand." This malleable phrase would have left the issue of the Board's jurisdiction unresolved. The Board suggests in its brief that it proposed the change in language that Congress eventually adopted in 1966, but this is not the case.[29] Nor is it accurate to say, as the Board states in its brief, that "[t]he Board's proposal was in substance enacted." Pet. Br. at 29.

Indeed, Congress rejected any form of words that might confer on the Board the latitude to expand the scope of the language of Congress, and did this by including in the 1966 amendments a new and narrower definition of bank that focused entirely on the *legal rights* of the depositor. The new definition, which was supplemented but not changed by the 1970 amendments, defined a "bank" for purposes of the BHCA as "any institution that accepts deposits that the depositor has the legal right to withdraw on demand." Pub.L. No. 89-485, § 2(c), 80 Stat. 236 (1966).

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[29]The Board implies, Pet. Br. at 29, that it submitted compromise statutory language that included "checking accounts" as the defining element of a demand deposit. However, in reality, the Board's proposed statutory language referred only to "deposits payable on demand" and made no reference to checking accounts. Letter of J. L. Robertson, (April 20, 1966), *reprinted in Amend the Bank Holding Company Act; Hearings supra* note 11, at 447.

Thus, Congress rejected the Board's "functional" reconstruction of its 1956 language and substituted a definition that acquired precision through its focus on the legal rights of the depositor. Whether a depositor has a legal right to withdraw his deposit on demand, of course, may be ascertained with specificity. As such, any latitude the Board might have had to place an "actual practice" interpretation on this language was eliminated.

In the matter now before this Court, however, the Board has again attempted to interpolate an "actual practice" standard into a specific congressional formulation. This time, the Board contends that NOW accounts are the "functional equivalent" of "deposits that the depositor has the legal right to withdraw on demand" because in "actual practice" depository institutions do not exercise their own reserved right to reject such a demand withdrawal. Pet. Br. at 33. But this effort to read a functional equivalence concept into language chosen for its legal specificity clearly evades the purpose of Congress.

Moreover, although the Board attempts, Pet. Br. at 28-29, to minimize the significance of its reversal by Congress in 1966, the legislative history demonstrates that Congress chose to redefine bank as it did because it wanted to leave no latitude for the Board to expand the BHCA to the corporate owners of depository institutions other than commercial banks. The Senate Report on the 1966 amendments sheds light not only on the demand deposit language but also on the purposes of the BHCA as a whole:

> *The purpose of the act was to restrain undue concentration of control of commercial bank credit, and to prevent abuse by a holding company of its control over this type of credit for the benefit of its nonbanking subsidiaries.* This objective can be achieved without applying the act to savings banks, and there are at least a few instances in which the reference to "savings bank" in the present definition may result in covering companies that control two or more industrial banks. To avoid this result the bill redefines "bank" as an institution that accepts deposits

> payable on demand (checking accounts), *the commonly accepted test of whether an institution is a commercial bank* so as to exclude *institutions like* industrial banks and nondeposit trust companies.

S. Rep. No. 1179, *supra* note 6, at 7 (emphasis added).

Congress could not have been more direct: the purpose of the BHCA was to control commercial banks. Institutions that were not commercial banks were not to be covered; in order to be sure that *only* commercial banks *were* covered, these institutions were defined with reference to their distinguishing feature — the acceptance of demand deposits that the depositor has a legal right to withdraw on demand.

Thus, Congress did not adopt the demand deposit formulation in 1966 in order to cover all institutions that offered accounts accessible by check, but as a short-hand method of defining commercial banks, the only institutions intended to be subject to the BHCA.

D. 1970 Amendments

1. Application of the BHCA to One-Bank Holding Companies

Not long after Congress affirmed the exclusion of one-bank holding companies in 1966, the courts rejected various rulings by the Comptroller of the Currency that had permitted expanded banking-related activities by national banks.[30] Large commercial banks began turning to one-bank holding companies as vehicles for extending their activities into related fields.[31] The significance of the one-bank holding company form

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[30] *See, e.g., Saxon v. Georgia Ass'n of Indep. Ins. Agents*, 399 F.2d 1010 (5th Cir. 1968) (Comptroller did not have the authority to allow national banks to act as insurance agents in locations exceeding 5,000 in population). *See also* Comment, *Implementation of the Bank Holding Company Act Amendments of 1970: The Scope of Banking Activities*, 71 Mich. L. Rev. 1170, 1173-76 (1973) (discussing frustration of Comptroller's efforts).

[31] *See, e.g.*, Chase, *The Emerging Financial Conglomerate: Liberalization of the Bank Holding Company Act*, 60 Geo. L.J. 1225, 1234, (1972) ("dramatic proliferation" of one-bank holding companies due, in part, to bankers' efforts to broaden their services through this more flexible corporate form).

thus changed dramatically. Nearly 900 new one-bank holding companies were created between 1965 and 1970, and the percentage of the nation's total banking deposits controlled by one-bank holding companies grew from less than 10% in early 1967 to more than 40% in 1969. Most significantly for Congress, the six largest commercial banks in the country, which cumulatively held more than 20% of the country's deposits, each formed a one-bank holding company during this period. S. Rep. No. 1084, *supra* note 6, at 2-3.

The increase in the use of the one-bank holding company by large commercial banks led to a concern in Congress that the rapid expansion of this corporate structure could lead to excessive concentration of commercial credit power as clusters of large commercial enterprises formed around large commercial banks. The 1970 amendments to the BHCA ensued. Although the Administration and the House Banking Committee each developed a bill, the Senate bill was substantially the version ultimately adopted.[32]

The congressional purpose behind the measure was articulated as follows by Senator Harrison Williams, a member of the Senate Banking Committee:

> The creation of large bank-originated one-bank holding companies is the sole reason for the legislation before us today. Businessmen fear disabling competition caused by large banks with their vast economic resources. Various proposals have been advanced to bring these banks under the regulatory framework. This is the purpose of . . . the Bank Holding Company Act amendments of 1970.

116 *Cong. Rec.* 32,107 (1970).

But concern about the power of the large commercial banks did not cause Congress to adopt the Board's theory that banking and commerce should be separated. When Congress brought one-bank holding companies under the BHCA, it took steps in the interest of preserving and extending competition

[32]*See, e.g.*, 116 *Cong. Rec.* 41,953 (1970) (statement of Rep. Widnall).

to assure that these firms were permitted to *expand* their commercial activities, although to a limited degree. Prior to 1970, the Board had limited the activities of each bank holding company to those businesses that were directly related to the activities of its particular subsidiary banks. The 1970 Amendments made important changes in the Board's authority under section 4(c)(8) of the Act that were intended to free the Board from these narrow precedents.

Far from separating banking and commerce, the principal congressional proponents of the 1970 amendments[33], commentators,[34] and even the Board, expected that these changes in the language of the BHCA would enable bank holding companies to expand their activities into areas of commerce "closely related to banking" but nevertheless not permissible to banks themselves.[35] In the words of Senator Sparkman (the Chairman of the Senate Banking Committee and the principal Senate conferee):

> The bill [agreed upon in conference] . . . provided the necessary flexibility of regulation and administration which the Federal Reserve Board requested in order to permit it to depart from past precedents and to permit expansion of bank and bank related activities which will be required in order to meet fully the rapidly expanding and varying financial needs of the economy of the Nation.

[33]Although the House managers of the bill interpreted the changed language in § 4(c)(8) to be more restrictive, *see* Statement of the Managers on the Part of the House, H.R. Rep. No. 1747, 91st Cong., 2d Sess. 11, 21–22 (1970), the Senate conferees, a minority of the House conferees, and the Board believed that the changes considerably expanded the latitude for bank holding companies to engage in non-banking activities. *See, e.g.*, 116 *Cong. Rec.* 42,422 (1970) (statement of Sen. Sparkman); 116 Cong. Rec. 41,953 (1970) (statement by Rep. Widnall); letter of Chairman of the Board of Governors Arthur Burns *reprinted in* H.R. Rep. No. 1747, *supra*, at 16.

[34]*See* Chase, *supra* note 26, at 1247.

[35]*See National Courier Ass'n v. Board of Governors of the Fed. Reserve Sys.*, 516 F.2d 1229, 1236 (D.C. Cir. 1975) (1970 amendments give Board greater discretion to permit bank holding companies to engage in nonbanking activities).

116 *Cong. Rec.* 42,422 (1970).

Arthur Burns, then the Board's Chairman, joined in support of the conference language:

> [W]e do not believe it is desirable to unduly restrict entry by nonbank subsidiaries into markets that are distinct from those served by the subsidiary banks of the holding company.

Letter to Chairman of the House Banking Committee, (Nov. 23, 1970), *reprinted in* 116 *Cong. Rec.* 42,423 (1970).

The Board itself moved quickly to permit regulated bank holding companies to enter areas of commerce ordinarily denied to banks.[36]

Thus, while Congress applied the BHCA to one-bank holding companies in 1970, it sought at the same time to enhance competition by permitting these institutions to enter new commercial activities, "closely related to banking" as defined by the Board. The fact that these new activities were to be limited in scope is consistent with a view of the BHCA as a statute intended to curb the economic power of commercial banks, and not to implement a policy of separating banking and commerce.

2. Definition of "Bank"

Returning again to its 1966 language (which defined "bank" as an institution that "accepts deposits that the depositor has a legal right to withdraw on demand"), Congress in 1970 added the further test "and engages in the business of making commercial loans."[37] The addition of a commercial loan requirement to language that Congress had carefully chosen in 1966 as a

[36]*See* Reg. Y, 36 Fed. Reg. 15,526 (1971). Today, such permissible activities include, *inter alia*, data processing services, underwriting credit life, accident and health insurance, courier services, management consulting, issuance and sale of savings bonds and travelers checks, real estate, appraisal, and acting as a futures commission merchant. *See* 12 C.F.R. § 225.25, 49 Fed. Reg. 826-28 (Jan. 5, 1984).

[37]Pub. L. No. 91-607, § 101(c), 84 Stat. 1760, 1762, 12 U.S.C. § 1841(c) (1970).

precise legal definition of commercial banking underscores a congressional purpose to apply the Act to a particular aspect of commercial banking.

The commercial loan requirement first appeared as part of a comprehensive bill to amend the BHCA, introduced in 1970 by Senator Edward Brooke of Massachusetts. 116 *Cong. Rec.* 14,818-22 (1970). The Board's brief completely misstates the facts of Senator Brooke's involvement in the debate over the 1970 amendments, implying incorrectly that Senator Brooke introduced only the commercial loan proviso and did so "without discussion or comment." Pet. Br. at 41.

In fact, the commercial loan proviso was part of a thoroughgoing reform bill, S. 3823, by which Senator Brooke proposed to eliminate the restrictions on nonbanking activities of a bank holding company if the holding company's subsidiary banks had no dealings with the customers or suppliers of their nonbanking affiliates. *See* S. 3823 at § 3. Senator Brooke explained that this would eliminate the possibility that commercial banks would misuse their commercial credit power to assist their holding company affiliates. *See* 116 *Cong. Rec.* 14,820 (1970) (statement of Sen. Brooke). The bill also contained special anti-tying provisions, which were intended to prevent a commercial bank's use of its credit granting powers to coerce customers into dealing with its nonbanking holding company affiliates. *See* S. 3823 at § 4. Thus, it was fundamental to Senator Brooke's proposal that commercial loans be understood to mean loans negotiated between a bank and a customer. Only in that case would it be possible for a commercial bank to favor its affiliates, and only in that case would anti-tying provisions be necessary.

Far from advancing his proposal "without discussion or comment," Senator Brooke's bill was accompanied by an extensive statement. 116 *Cong. Rec.* 14,818-22 (1970). As a member of the Senate Banking Committee, Brooke took an active part in hearings on the 1970 amendments and the floor debates.[38]

[38]*See, e.g., One-Bank Holding Company Legislation of 1970: Hearings on S. 1052, S. 1211, S. 1664, S. 3823 and H.R. 6778, Before the Senate Committee on Banking and Currency*, 91st Cong., 2d Sess. 150-51 (1970); 116 *Cong. Rec.* 32,127-33 (1970) (statements of Sen. Brooke).

Indeed, Senator Brooke's bill had considerable influence on the Senate bill ultimately reported out in September of 1970. His definition of "bank" was adopted by the Senate Banking Committee along with the anti-tying language he had also included in S.3823. *Compare* § 4 of S. 3823 *with* § 106 of Pub.L. No. 91-607 (1970). The Committee's report clearly adopted Senator Brooke's approach:

> The definition of "bank" adopted by Congress in 1966 was designed to include commercial banks and *exclude those institutions not engaged in commercial banking*, since the purpose of the Act was *to restrain undue concentration of commercial banking* resources and to *prevent possible abuses related to control of commercial credit*. However, the Federal Reserve Board has noted that this definition may be too broad and may include institutions *which are not in fact engaged in the business of commercial banking in that they do not make commercial loans*. The Committee, accordingly, adopted a provision which would exclude institutions that are not engaged in the business of making commercial loans from the definition of "bank."

S. Rep. No. 1084, *supra* note 6, at 24 (emphasis added).[39]

Moreover, it is highly significant to the issue now before this Court that Senator Brooke's language concerning commercial

[39]The Board asserts in its brief, without any support whatsoever, that the commercial loan proviso inserted in the 1970 amendments was "a technical amendment designed to create a narrowly circumscribed exclusion from the Act's coverage," Pet. Br. at 41, and implies, *id.* at 13 and 43, that the definition of "bank" proposed by S. 3823 was intended only to cover a single institution in Massachusetts — the parent of the Boston Safe Deposit and Trust Company ("Boston Safe"), a largely trust-service institution that also accepted demand deposits.

This hypothesis is inherently unrealistic and does not reflect the legislative history of the 1970 amendments. Although Senator Brooke's definition certainly had the effect of excluding Boston Safe from the BHCA, it was intended to do much more. If Senator Brooke had intended solely to exempt Boston Safe from the Act he would not have introduced and consistently argued for a comprehensive bill; all that would have been necessary to achieve this narrower purpose was, *e.g.*, an exemption for trust companies that accepted demand deposits incidental to their trust activities.

loans was intended to cover commercial lending in the traditional, accepted sense, *i.e.*, a bank's making commercial credit available to a customer in a negotiated transaction that could involve tying or other abuses. In its brief, the Board itself describes potential "abuses" of commercial credit, such as preferential allocation of credit. *See* Pet. Br. at 21. These abuses can occur only when a commercial bank makes a loan directly to a particular customer,[40] and they do not arise when a bank purchases money market instruments in the open market. That Congress held the same view is demonstrated by the reference in the Senate Report to "possible abuses related to control of commercial credit." S. Rep. No. 1084, *supra* note 6, at 24.

Much as it has done with its analysis of NOW accounts, *see* Pet. Br. at 26-38, the Board has based the regulatory reversal challenged in this case on a tortured "functional" reconstruction of what Congress meant by "the business of making commercial loans." Once again the Board asserts that an activity Congress did not mention is functionally equivalent to or otherwise the same as something to which Congress did specifically refer. Thus, the Board advances the proposition that a bank's transactions in the money market, such as purchasing commercial paper, bankers' acceptances and certificates of deposit, are a "permissible construction" of the term "commercial loan." Pet. Br. at 39. But Senator Brooke's use of the term commercial loan, and the use clearly contemplated by Congress at the time, was a more limited and customary definition. Indeed, the Board itself implemented this definition for many years,[41] only

[40]Indeed, in a 1966 letter to Sen. Robertson, the Board's Chairman, indicated his support for language limiting the BHCA soley to banks that make commercial loans: "I am impressed by the argument that a bank that does not make commercial loans is not apt to be involved in the kind of abuses the Act is designed to prevent." *Reprinted in* 112 *Cong. Rec.* 12,386 (1966).

[41]Until 1982, the Board's test for defining "commercial loan" distinguished between "passive" media of investment and the close "lender-borrower relationship that is one of the characteristics of commercial loans, and which presents the possiblity of abuses relating to the control of commercial credit that concerned the Congress when it adopted the commercial lending test found in the Act." Letter to William McDonough, Ass't. General Counsel, Federal Reserve Bank of Boston, from Robert E. Minton, Deputy General Counsel, at 2 (November 13, 1980) (J. A. 105A).

reversing its interpretation when it sought a basis for inhibiting the development of non-BHCA banks.

Thus, the 1970 Amendments to the BHCA clearly follow the pattern established in 1956 and 1966. The Act was modified to address a new manifestation of the economic power of large commercial banks. To avoid excessive restrictions on competition, Congress sought to *expand* the range of commercial activities permitted to regulated bank holding companies newly brought under the BHCA. Congress also amended the definition of "bank" to emphasize that while the BHCA was intended to apply to commercial banks, it was the potential abuses inherent in a commercial bank's relationship with its loan customers, such as tying, that were of particular concern.

Thus, the Board's efforts to expand the concept of "commercial loan" in Regulation Y, and to support its revisions of Regulation Y with generalizations concerning the separation of banking and commerce, are inconsistent with the Amendments to the BHCA adopted by Congress in 1970.

E. Congressional Action after 1970

The actions of Congress in the Garn-St Germain Depository Institutions Act of 1982 ("Garn-St Germain"), underscores the fact that Congress has never adopted a policy of separating banking and commerce.

In Garn-St Germain, all federally chartered savings and loan associations and federal savings banks were for the first time given authority to make commercial loans up to 10% of their assets, *See* Pub. L. No. 97-320, § 325, and to establish demand accounts for commercial customers with which they have established a commercial loan relationship. *Id.*, § 312.

The combination of commercial lending and demand deposit powers brought these thrift institutions squarely within the definition of "bank" under the BHCA and would have subjected their holding companies to the strictures of the BHCA. If, as the Board suggests, Congress had adopted and intended to pursue a national policy of separating banking and commerce, this is exactly the result one would have expected. But Con-

gress has been concerned about the enhancement of the economic power that inheres in the concentration of commercial credit resources, not about the separation of banking and commerce. Because thrift institutions offered no significant threat of monopolizing commercial credit, Congress saw no reason to subject them to the regime of the BHCA, even though they were now able to exercise (to a limited degree) all of the powers of commercial banks. Thus, in Section 333 of Garn-St Germain, 12 U.S.C. § 1841(c), Congress exempted a whole class of thrifts from the BHCA[42], permitting their holding companies to be regulated solely under the Savings and Loan Holding Company Act, 12 U.S.C. § 1730a, which imposes no restrictions on the holding companies of a single thrift institution.[43]

It is also particularly instructive for this case that Congress chose in Garn-St Germain to link commercial lending and demand accounts. In 1980, savings and loans had been authorized to offer NOW accounts to individuals. Depository Institutions Deregulation and Monetary Control Act of 1980, Pub. L. No. 96-221, § 303, 94 Stat. 132, 146, 12 U.S.C. § 1832(a). In Garn-St Germain, rather than extend NOW accounts to commercial customers of thrifts, Congress authorized demand accounts for these customers. That choice demonstrates that Congress understands the difference between demand accounts and NOW

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[42]Under Garn-St Germain, the exemption from the BHCA is effective if the thrift institution qualifies as a domestic building and loan association under Section 7701(a)(19) of the Internal Revenue Code of 1954, 26 U.S.C. § 7701(a)(19). Generally, at least 60% of the assets of a qualifying domestic building and loan association must consist of cash, residential mortgage loans, time and demand deposits with financial institutions, obligations of the United States or political subdivisions, educational loans and other specified instruments.

[43]As Congress was aware when granting commercial lending authority to thrifts in 1982, commercial companies had long owned savings and loan associations. Indeed, Sears, Roebuck and Co. has been a savings and loan holding company for over 25 years by virtue of its control of an insured institution in California. The Ford Motor Company recently announced that it intends to acquire First Nationwide Federal Savings & Loan Association, one of the nation's largest thrift institutions. *See* Am. Banker, Aug. 2, 1985, at 1, col. 4.

accounts and does not use these terms interchangeably in legislation.

CONCLUSION

For decades, the Federal Reserve Board has sought to extend its authority over the holding companies of the nation's depository institutions. Its central theme has been the "separation of banking and commerce." The Board has urged this policy on Congress so often and so persistently that the Board seems actually to believe that such a policy has been adopted.

Congress, on the other hand, has been equally persistent in avoiding the establishment or implementation of an overarching and inflexible "principle" such as separating banking and commerce. Instead, it has sought simply to restrain the economic power of commercial banks, acting to deal with each specific manifestation of this power as it arose, and going no further than necessary to achieve its limited objectives. Thus, despite recurring demands by the Board, Congress has been moved to address bank holding companies only in response to external events that were widely perceived to portend major enhancements of the economic power of commercial banks. Examples include the denial of the Board's Clayton Act prosecution against Transamerica Corporation in 1953 and the rapid movement of large commercial banks into one-bank holding companies after 1968.

Particularly since 1980, the Board has repeatedly stressed the urgency of enacting legislation that would bring non-BHCA banks under the Act. Congress has remained unmoved. Impatient to achieve its ends, however, and pursuing its own vision of how the financial services system should be organized and regulated, the Board has attempted in the regulatory action challenged in this case to arrest the development of non-BHCA banks. In order to reach institutions that it now regards as undesirable, the Board has unilaterally attempted to expand its own authority without the participation of the Branches of Government created by Articles I and II of the Constitution and it has done so once again by placing its own unauthorized

gloss on statutory language carefully chosen by Congress for its specificity and precision.

The high-sounding cloak for this usurpatory action is a mythic "national policy" of separating banking and commerce. This Court should not lend its imprimatur to a policy that the Board alone has adopted, or to the unauthorized regulation issued in its name.

For these reasons, this Court should affirm the decision of the court below.

Respectfully submitted,

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